

## THE HOMEOWNERS PROTECTION ACT OF 1998

### Yes, you can cancel your private mortgage insurance.

On July 29, 1998, President Clinton signed into law a bill, The Homeowners Protection Act of 1998, that will make it easier for homeowners to free themselves from private mortgage insurance (PMI) payments and reform the PMI system.

PMI was created so that people can buy homes without having to first amass large amounts of cash. Mortgage lenders require homebuyers to take out PMI if the buyers put less than 20 percent down when they take out the mortgage. It protects the lender against losses if a homeowner defaults on the mortgage.

Unlike other kinds of insurance, PMI does not benefit the person who pays for it; it benefits the lender instead. On average, homeowners pay between \$240 and \$1,200 a year in PMI premiums.

In theory, homeowners should be able to cancel their PMI once they've established at least 20 percent equity in their home (that's because homeowners who have invested heavily in their homes are far less likely to default on their mortgages). Usually, one establishes equity by paying steadily into a mortgage, although rising and falling real estate values can affect equity levels as well.

Savvy homeowners who want to drop PMI have found it harder than they'd thought, and many more may never even know that they have the option of dropping the coverage.

### WHAT THE NEW LAW DOES

The Homeowners Protection Act of 1998 will allow homeowners with good payment records to request that their PMI be cancelled once they have 20 percent equity (in other words, once they've paid off 20 percent of their total mortgage). If your house soars in value, that won't count. The 20 percent equity is measured against the value of the house the day you bought it.

It requires that PMI be automatically terminated once that equity rises to 22 percent. It also requires lenders to disclose more information about PMI, what it does, and when it can be cancelled and notice/disclosure of cancellation rights with respect to PMI which is required as a condition for entering into a residential mortgage transaction.

### What the new law doesn't do

The new law took effect July 29, 1999 (a year after Clinton signed it) and only newly written PMI policies will be subject to the automatic-termination provision. **Furthermore, the bill doesn't cover mortgage insurance provided through the Federal Housing**

**Administration.** Certain types of loans considered to be "high-risk" may have different provisions.

### PMI CANCELLATION CIRCUMSTANCES

There are two circumstances under which the holder of a mortgage must cancel or terminate the private mortgage insurance requirement of a mortgagor. There is also a "high-risk" exemption from these cancellation requirements.

The cancellation / termination provisions apply only to:

1. mortgages made one-year after date of enactment and
2. mortgages on owner occupied single-family primary residences.

### Borrower-initiated Cancellation...

When a mortgage that is subject to PMI reaches an 80% loan-to-value ratio; loan to value (LTV) based upon the initial amortization schedule or pre-payments, the borrower may make a written request that PMI be canceled.

For adjustable rate mortgages, the cancellation or termination will be based on "amortization schedules" rather than the initial amortization schedule.

The mortgage holder must cancel the PMI if the following conditions are met:

1. the borrower has a good payment history (no mortgage payment 60 days or longer past due in the 12 month period beginning 24 months before the cancellation date or a payment 30 days or longer past due in the immediately preceding 12 months;
2. the mortgage-holder approved verification of property value; and
3. the certification that the property's equity is unencumbered by a subordinate lien.

### Automatic Termination...

When a mortgage that is subject to PMI reaches a 78% (LTV) as a result of the initial amortization schedule, the **PMI must be automatically terminated provided that the borrower is current on payments**. If the borrower is not current, the PMI must be automatically terminated when the borrower becomes current. With a 30 year mortgage, it will take eight or ten years on average to reach the point where you can cancel the insurance.

If the loan is determined to be a **"high-risk" loan**, cancellation and automatic termination is delayed until the loan reaches its half-life in the case of conforming loans, and 77% LTV or its half-life, whichever occurs first, in the case of all other high-risk loans. "High-

risk" will be defined by Fannie and Freddie in published guidelines for loans that do not exceed the applicable annual conforming loan limit and mortgagees for all other loans.

### Final Termination...

There is final termination if the requirement for PMI is otherwise cancelled or terminated in accordance with Borrower Cancellation or Automatic Termination. In no case may such requirement be imposed beyond the first day of the month immediately following the date that is the midpoint of the amortization period of the loan if the mortgagor is current on the payments required by the terms of the mortgage.

### DISCLOSURE / NOTIFICATION REQUIREMENTS

The legislation requires:

1. disclosure and annual notices of cancellation / termination information to borrowers for new mortgages,
2. an annual notice to existing mortgage holders, and
3. notification upon cancellation or termination of PMI.

### New Mortgages...

Effective one year after the date of enactment (July, 1999) new disclosures will be required at time of transaction for new mortgages that require PMI.

### FIXED RATE MORTGAGE DISCLOSURES

◆ A written initial amortization schedule; and written notice- that the mortgagor may cancel the requirements in accordance with the section on Borrower Cancellation of the Act indicating the date on which the mortgagor may request cancellation, based solely on the initial amortization schedule;

◆ that the mortgagor may request cancellation in accordance with the section on Borrower Cancellation earlier than provided for in the initial amortization schedule based on actual payments;

◆ that the requirement for PMI will automatically terminate on the termination date in accordance with the section on Automatic Termination and what that termination date is with respect to that mortgage; and

◆ that there are exemptions to the right to cancellation and automatic termination of the requirement for PMI in accordance with the section on Exceptions for High Risk Loans and whether such an exemption applies at that time to that transaction.

## ADJUSTABLE RATE MORTGAGE DISCLOSURES

- ◆ The mortgagor may cancel the requirement in accordance with the section on Borrower Cancellation, on the cancellation date and that the servicer will notify the mortgagor when the cancellation date is reached;
- ◆ the requirement for PMI will automatically terminate on the termination date and that on the termination date, the mortgagor will be notified of the termination or that the requirement will be terminated as soon as the mortgagor is current on loan payments; and
- ◆ there are exemptions to the right of cancellation and automatic termination of the requirement for PMI in accordance with the section on Exceptions for High Risk Loans and whether such an exemption applies at that time to that transaction.

## EXCEPTED TRANSACTION DISCLOSURES

In the case of Exceptions for High Risk Loans, at the time at which the transaction is consummated, the mortgagee shall provide written notice to the mortgagor that in no case may PMI be required beyond the date that is the midpoint of the amortization period of the loan, if the mortgagor is current on payments required by the terms of the residential mortgage.

## ANNUAL DISCLOSURES

If PMI is required in connection with a residential mortgage transaction, the servicer shall disclose to the mortgagor in each transaction in an annual written statement--

- ◆ the rights of the mortgagor under the Act of cancellation or termination of the PMI requirement; and
- ◆ an address and telephone number that the mortgagor may use to contact the servicer to determine whether the mortgagor may cancel the PMI.

## EXISTING MORTGAGE HOLDERS

For existing mortgages (mortgages entered into prior to one-year after the date of enactment), the mortgage holder must provide the borrower with an annual written statement that the PMI may, under certain circumstances, be canceled by the borrower with the consent of the mortgage holder; and includes an address and telephone number the borrower may use to contact the servicer to determine whether the borrower may cancel PMI.

These disclosures and annual notices may be provided as part of either the annual disclosure related to the escrow account or the annual disclosure of interest payments made pursuant to IRS regulations. In addition, no fees may be charged for providing disclosures or notices required under the Act.

If an otherwise eligible borrower did not meet the requirements for cancellation or termination of PMI, written notice must be provided

to the borrower, not later than 30 days after the cancellation request or termination date, stating the grounds for such determination.

## NOTIFICATION UPON CANCELLATION OR TERMINATION - NO FURTHER PAYMENTS

Upon cancellation or termination of PMI the mortgage holder/servicer must notify the borrower in writing (not later than 30 days after the cancellation or termination date) that: PMI has terminated and the borrower no longer has PMI; and no further premiums, payments, or other fees shall be due or payable by the borrower in connection with PMI.

## RETURN OF UNEARNED PREMIUMS

In general, not later than 45 days after the termination or cancellation requirement under this section, all unearned premiums for PMI shall be returned to the mortgagor by the servicer. If a mortgage insurer is in possession of any unearned premiums, the mortgage insurer shall transfer an amount equal to the amount of the unearned premiums to the servicer of the subject mortgage to be returned to the mortgagor not later than 45 days after receipt of the refund.

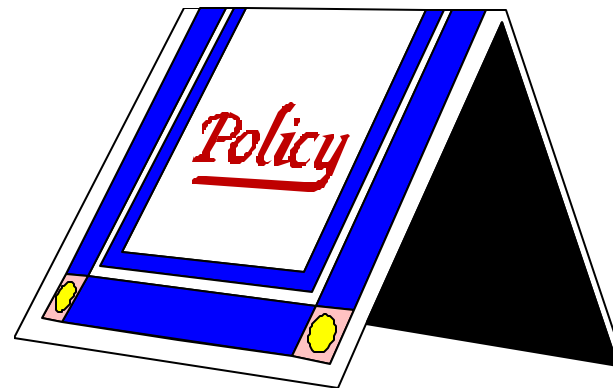
## EXCEPTIONS FOR HIGH RISK LOANS

The termination or cancellation provisions do not apply to any residential mortgage or mortgage transaction that, at the time at which the residential mortgage transaction is consummated, has high risks associated with the extension of the loan:

- ◆ As determined in accordance with guidelines published by Fannie Mae and Freddie Mac, in the case of a mortgage loan with an original principal balance that does not exceed the applicable conforming loan limit for the secondary market established by section 305(a)(2) of the Federal Home Loan Mortgage Corporation Act, so as to require the imposition or continuation of PMI requirement beyond the terms specified in Borrower Cancellation and Automatic Termination; or
- ◆ as determined by the mortgagee in the case of any other mortgage, except that termination shall occur-- with respect to a fixed rate mortgage, on the date on which the principal balance of the mortgage, based solely on the initial amortization schedule for that mortgage, and irrespective of the outstanding balance for that mortgage on that date, is first scheduled to reach 77% of the original value of the property securing the loan; and
- ◆ with respect to an adjustable rate mortgage, on the date on which the principal balance of the mortgage, based solely on amortization schedules for that mortgage, and irrespective of the outstanding balance for that mortgage on that date, is first scheduled to reach 77% of the original value of the property securing the loan.



# PRIVATE MORTGAGE INSURANCE



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